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SENSITIVE

BUDAPEST FOR KARYN POSNER-MULLEN

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TAGS: [SENV](#) [EIND](#) [EZ](#) [EUN](#)

SUBJECT: COAL CASH - CZECH EMISSION TRADING PLAN: DRAFTED BY BUSINESS, FOR BUSINESS, WITH THE UNPRECEDENTED SUPPORT OF BOTH THE GOVERNMENT AND THE OPPOSITION.

Sensitive but Unclassified -- not for Internet distribution.

11. (U) SUMMARY. The Czech Republic has proposed to the EU an emissions trading scheme that increases the ceiling on emissions above current levels. Environmental groups point to conflicts of interest, say the Czech proposal ignores submission criteria and the government's own stated energy policy, and argue it amounts to massive subsidies to state-run and private firms; the Environment Ministry echoes this view. But governing left-of-center Social Democrats have come down firmly on the side of business, and the Ministry of Industry and Trade largely dictated the terms of the Czech proposal. Because of their delay in submitting a proposal for vetting, the Czech Republic will not be a part of the EU emissions trading scheme when it begins January 1. End Summary

12. (U) The sectors of Czech industry that will participate in the emissions trading scheme have historically emitted approximately 89 million tons of CO2 annually. Environmental NGOs, in the spirit of the Kyoto Protocol, asked the government to submit a National Allocation Plan (NAP) under the EU's emissions trading scheme of 85 million tons, a small reduction. However, the latest version of the Czech's NAP, which won't be approved by the European Commission in time for the January 1, 2005 start of the trading scheme, sets allocations levels at 107.6 million tons, an increase of roughly 21 percent.

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POTENTIAL TO REDUCE COAL CONSUMPTION NOT INCLUDED IN NAP  
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13. (U) The Czech Republic gets approximately 80 percent of its electricity from power plants that burn a soft form of coal. The State energy plan had called for some of the dirtiest coal burning plants to be retired as the nuclear plant at Temelin came on line, or by 2010 at the latest. Temelin's two reactors have just finished their trial period and are now operating at full capacity. Nearly all of their output is exported. In fact, the Czechs are now the 7th biggest exporter of electricity in the world. But none of the coal-fired plants have been shut down, nor have the reductions in coal consumption that these shutdowns would bring been included in the NAP, even though these shutdowns are part of the government's published energy policy.

14. (U) Other potential reductions could be found in wasteful heating systems, and the old communist-era factories. Older Czech buildings and the water pipes that deliver heat are badly insulated. Many factories could reduce emissions simply by switching fuel from coal to gas. But once again, there is no assumption in the NAP that any reductions will occur.

15. (U) The Czech NAP was drawn up by the Ministry of Industry and Trade, which has not revealed the methods it used to arrive at the figure of 107.6 metric tons. The business community was consulted. The government then cited business confidentiality as the reason for excluding NGOs from the

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process. Just under two-thirds of the allocations would go to the energy sector, the main company of which, CEZ, has the Czech government as its main shareholder. Another beneficiary would be the commercialized firm, Viltcovice Steel, which also has the state as its main shareholder. As one environmental NGO pointed out, the Czech government has no incentive to force itself to make costly changes and reduce emissions at state-run firms. On the contrary, surplus allocations of 18.6 million tons a year, if the market price stays near the current value of 9 Euro, could mean an extra 220 million dollars a year for Czech firms.

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CREATING A MARKET WHEN YOU'RE THE ONLY PLAYER  
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16. (U) Last year the world's biggest emissions and coal

brokerage firm, Evolution Markets, teamed up with a Slovak Firm, Menert, to form Evolution Menert. This firm advised several Central European governments, including the Czechs, on how to draft a NAP. The firm, which has offices in Bratislava and Prague, is currently the only emissions broker in the two countries. It stands to make healthy profits off the trade of surplus allocations. As the firm's own web page points out, "Slovakia and the Czech Republic are positioned to be major participants in global greenhouse gas markets. Both countries are currently well below their greenhouse gas emission reduction targets under the Kyoto Protocol. In addition, Slovak and Czech government officials are encouraging investment in their energy infrastructure that will not only improve services, but also reduce overall levels of greenhouse gas emissions."

17. (U) Environmentalists ask why, if the Czech Republic is already below its emissions target, and the government is encouraging further reductions in the levels of emissions, did the government and Evolution Mennert draft a plan with emission allocations 21 percent higher than the target? Ivo Mravinac, the spokesperson for the Ministry of Industry and Trade offered one answer to this question: "It's useful for the firms to have permission for emissions at higher levels so that if they do not use up their quota, they could trade the remainder with other countries."

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MINISTRY OF INDUSTRY AND TRADE  
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18. (SBU) The Czech emissions trading proposal has touched off debate between government ministries, but there has been little political debate. Both major political parties -- the center-left Social Democrats, who lead the governing coalition, and the center-right Civic Democrats, who are the main opposition party and generally practice a policy of zero tolerance towards the government -- support the proposed scheme. Large Czech businesses, which initially opposed the emissions trading scheme, but now embrace it having realized the potential windfall it represents. On the political scene, matters came to a head on November 2nd when the lower house of parliament undertook the second reading of a bill that would set conditions for participation in the scheme. The Ministry of the Environment had insisted that any revenues generated by the sales of allowances be spent on green technologies. But a coalition of pro-business forces defeated this motion. The Minister of the Environment, Libor Ambrozek, felt that parliamentarians from both the government and opposition were conspiring, along with the directors of the nation's largest industrial firms and the Ministry of Industry and Trade, to draft a bill that would favor business at the cost of the environment. He sent the company directors SMS messages saying "the changes have undoubtedly been prepared by you and the Ministry of Industry and Trade." Ambrozek, a Christian Democrat normally considered a soft spoken gentleman, included a vulgar expression in his SMS, which touched off calls for his resignation by one member of parliament's committee on trade.

19. (SBU) The Czech Plan is one of 4 NAPs that the European Commission must still approve. Poloff spoke with Dr. Jiri Hlavacek, a special advisor to the Minister of the Environment about the Czech NAP's chances in Brussels. He acknowledged that most of the new EU states have had their NAP proposals cut by 20 percent, but added, "We are prepared to go to Brussels and fight for this." However, others at the ministry confided to Poloff that, "He has to say this, although the current plan is politically indefensible."

11. (SBU) Comment: We can only wait and see how far the European Commission will cut back on the Czech NAP. But it seems clear enough that the Czechs are not hoping for a market-based method of producing the most cost-effective reductions in greenhouse gases. Instead, it appears that they, as was the case with other members of the former Soviet Bloc, see the scheme as a distortion of market forces, that might allow some Czech firms, including those run by the state itself, to reap windfall profits while avoiding the reductions in emissions that are the principal reason for the scheme's existence.  
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